KOPERASI RAKYAT BHD

v.

HARTA EMPAT SDN BHD

FEDERAL COURT, KUALA LUMPUR
WAN ADNAN ISMAIL CJ (MALAYA)
ZAKARIA YATIM FCJ
GOPAL SRI RAM JCA
[CIVIL APPEAL NO: 02-10-1997(A)]
25 MARCH 2000

CIVIL PROCEDURE: *Judicial precedent - Court of Appeal - Stare decisis - Certainty - Reversing earlier decision of another division of the same court - When departure can be made - Whether decision contained serious errors - Obiter dicta - Per incuriam*

COMPANY LAW: *Directors - Loans - Loan to director by third party - Security by way of charge provided by director's company - Whether charge void and unenforceable - Companies Act 1965, s. 133 - Whether breach of s. 133 invalidated the charge*

The plaintiff was in need of capital to develop several pieces of its land ('the land'). The plaintiff once applied to the defendant for a loan but its application was not approved because it was not a member of the defendant. The plaintiff wanted to get around this and subsequently resolved to create a first legal charge over the land in the defendant's favour for the purpose of securing a loan for one Lim Chin Hin, who was at all material times, a director of the plaintiff. Later on the plaintiff took out an originating summons claiming a declaration that the charge in the defendant's favour was void and unenforceable pursuant to s. 133 Companies Act 1965. The summons was dismissed by the judge at first instance. The plaintiff appealed to the Court of Appeal which reversed the judge's decision and overcame the Federal Court decision in *Feyen No 1* that a security given in contravention of s. 133 Companies Act 1965 was not void, by saying that the remarks were purely *obiter.*

Held:
Per Gopal Sri Ram JCA

[1] Certainty in law is one of the pillars upon which our justice system rests. Therefore, as a matter of public policy, it is not open to the Federal Court to reverse a decision of another division of the Federal Court given so recently. Great care must be taken especially in a case as the present which concerned the interpretation of a statutory provision. It should not be done save in the most exceptional of cases. Otherwise it would lead to uncertainty.

[2] Departure may be warranted in a case where it appears patently clear that the earlier decision was given in defiance of an express statutory provision that was overlooked by the court or where a serious error embodied in the decision of the court has distorted the law.

[3] The court agreed entirely with the reasoning in *Feyen No 1* that s. 133 Companies Act 1965 does not invalidate a security given in contravention of that provision.

[Appeal allowed; High Court order restored.]

*[**Bahasa Malaysia** Translation Of Headnotes]*

Plaintif memerlukan modal untuk membangunkan beberapa bidang tanah kepunyaannya ('tanah tersebut'). Plaintiff pernah memohon satu pinjaman daripada defendan tetapi permohonannya itu tidak diluluskan kerana ia bukan seorang ahli defendan. Plaintif ingin mengelak dari masalah tersebut lalu berkeputusan untuk membuat satu gadaian pertama pada tanah tersebut memihak kepada defendan untuk tujuan menjamin satu pinjaman kepada seorang Lim Chin Hin, yang mana pada kesemua masa matan, seorang pengarah plaintif. Selepas itu, plaintif telah mengeluarkan satu saman pemula menuntut satu perisytiharan bahawa gadaian yang memihak kepada defendan tak sah dan tidak boleh dikuatkuasakan selaras dengan s. 133 Akta Syarikat 1965. Saman tersebut telah ditolak oleh hakim bicara. Plaintif merayu ke Mahkamah Rayuan. Mahkamah mengakas keputusan hakim bicara dan mengatasi keputusan Mahkamah Persekutuan dalam *Feyen No 1* yang jaminan yang diberikan bertentangan dengan s. 133 Akta Syarikat 1965 bukan tak sah dengan mengatakan bahawa pendapat tersebut hanyalah *obiter.*

Diputuskan:
Oleh Gopal Sri Ram HMR

[1] Kepastian dalam undang-undang adalah merupakan satu tiang seri bagi sistem kehakiman kita. Dari itu, sebagai satu polisi awam, ianya tidak terbuka bagi mahkamah untuk mengakas satu keputusan yang baru sahaja diberikan oleh mahkamah bahagian lain. Perhatian yang teliti mestilah diberikan terutamanya dalam sesuatu kes seperti kes semasa yang berkenaan dengan pentafsiran satu peruntukan statut. Ianya tidak wajar dilakukan melainkan dalam kes yang luarbiasa. Jika tidak ianya akan menyebabkan ketidakpastian.

[2] Penyimpangan mungkin berasas di dalam kes dimana ianya tampak begitu jelas yang keputusan terdahulu telah melanggarkan satu peruntukan nyata statut yang tidak diendahkan oleh mahkamah atau dimana keputusan mahkamah itu mengandungi kesilapan serius yang telah memesongkan undang-undang.

[3] Mahkamah bersetuju secara bulat-bulat dengan taakulan di dalam *Feyen No 1* yang bahawa s. 133 Akta Syarikat 1965 tidak mentaksahkan jaminan yang diberi bertentangan dengan peruntukan tersebut.

[Rayuan dibenarkan; Perintah Mahkamah Tinggi dikembalikan.]

Case(s) referred to;

Chung Khiaw Bank Ltd v. Hotel Rasa Sayang Sdn Bhd [1990] 1 CLJ 675 ***(refd)***

Co-operative Central Bank Ltd (In receivership) v. Feyen Development Sdn Bhd (No 1) [1995] 4 CLJ 300 ***(foll)***

Co-operative Central Bank Ltd (In receivership) v. Feyen Development Sdn Bhd (No 2) [1997] 3 CLJ 365 ***(foll)***

Lori (M) Bhd (Interim receiver) v. Arab-Malaysian Finance Bhd [1999] 2 CLJ 997 ***(refd)***

R v. Shivpuri [1986] 2 All ER 334 ***(refd)***

Legislation referred to:

Companies Act 1965, ss. 67(1), (6), 133(1), (5)

For the appellant - CV Das (John Matthew with him); M/s TH Su & Co

For the respondent - Hira Singh (Abu Bakar Awang with him); M/s Asbir Hira Singh & Co

Reported by Izzaty Izzuddin

JUDGMENT

Gopal Sri Ram JCA:

An understanding of the background of this case is essential in order to properly appreciate the issues that have arisen for decision in this appeal. Fortunately, I am spared the task of dealing with the factual matrix at any great length as it has been detailed in the judgment of the learned trial judge. A summary of the relevant facts therefore suffices.

The respondent (whom I shall refer throughout this judgment as "the plaintiff") is a private company limited by shares. It carries on the business of housing development. It owns several pieces of land ("the subject property"). It wanted to develop the subject property into a housing estate. It was in need of capital to fund the development. It wanted to raise monies against the security of the subject property. However, the subject property was already charged to a finance company to which the plaintiff owed almost RM2 million.

The appellant (whom I shall refer to as "the defendant") is a co-operative society whose business and affairs are regulated by its own by-laws and the provisions of the Co-operative Societies Act 1948 ("the Act"). In June 1985, the plaintiff applied to the for a loan of RM5 million. But the plaintiff was not a member of the defendant. And s. 30 of the Act authorises loans only to members of a co-operative society. The plaintiff's application for a loan was therefore not approved by the defendant. The plaintiff wanted to get

around this difficulty. On 29 June 1985, it resolved, *inter alia*, to create a first legal charge over the subject property in the defendant's favour for the purpose of securing a loan of RM5 million to one Lim Chin Hin ("Lim"). Lim was, at all material times, a director of the plaintiff.

Then, on 19 August 1985, Lim applied to become a member of the defendant. His application was approved. Lim then applied for and obtained a loan of RM5 million from the defendant. A part of the loan amount was utilised to discharge the charge in favour of the finance company and to redeem the issue documents of title to the subject property. The plaintiff then executed a third party charge in the defendant's favour to secure the loan.

On 2 December 1991, the plaintiff took out an originating summons claiming a declaration that the charge in the defendant's favour was void and unenforceable. It relied on s. 133 of the Companies Act 1965 ("the Act"). That section reads as follows:

> 133(1) A company (other than an exempt private company) shall not make a loan to a director of the company or of a company which by virtue of section 6 is deemed to be related to that company, or enter into any guarantee or provide any security in connection with a loan made to such a director by any other person but nothing in this section shall apply:
>
> (a) subject to subsection (2), to anything done to provide such a director with funds to meet expenditure incurred or to be incurred by him for the purposes of the company or for the purpose of enabling him properly to perform his duties as an officer of the company;
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> (b) to anything done to provide such a director who is engaged in the full-time employment of the company or its holding company, as the case may be, with funds to meet expenditure incurred or to be incurred by him in purchasing or otherwise acquiring a home; or
>
> (c) to any loan made to such a director who is engaged in the full-time employment of the company or its holding company, as the case may be, where the company has at a general meeting approved of a scheme for the making of loans to employees of the company and the loan is in accordance with that scheme.
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> (4) Where a company contravenes this section any director who authorises the making of any loan, the entering into of any guarantee or the providing of any security contrary to this section shall be guilty of an offence against this Act.
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> Penalty: Ten thousand ringgit.
>
> (5) Nothing in this section shall operate to prevent the company from recovering the amount of any loan or amount for which it becomes liable under any guarantee entered into or in respect of any security given contrary to this section.

The plaintiff's summons came up before by P.S. Gill J, who, after hearing arguments declined to grant the declaration sought. He dismissed the plaintiff's summons with costs. He delivered a well reasoned and carefully considered judgment dealing with all the relevant points raised before him. This was on 12 September 1995.

Some 16 days later, on 28 September 1995, this court handed down its judgment in *Co-operative Central Bank Ltd (In receivership) v. Feyen Development Sdn Bhd.* [1995] 4 CLJ 300 *("Feyen No. 1")*. It dealt with the identical point. It held that a security given in contravention of s. 133 of the Act was not void. It was an authoritative pronouncement. It ought to have concluded the matter once and for all in the defendant's favour. But that was not to be.

The plaintiff was unhappy with the judgment of P.S. Gill J. It appealed to the Court of Appeal. That court reversed the learned judge. It overcame the decision in *Feyen No 1 (ibid)* by saying that the remarks upon the effect of s. 133(1) of the Act on a security were purely *obiter*. That appears clearly from the following passage in the judgment of the Court of Appeal:

> The subsection by itself does not invalidate the forbidden transactions, so that the company may incur civil liability for entering into them; see *Feyen*. However before the company can be made liable, the transaction itself must be a valid and enforceable one. In the instant case, we are concerned with a charge under the National Land Code 1965 ('the Code') so that the question that arises is whether the provisions of the Code operate to invalidate the charge.
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> *Feyen* did not refer to the provisions of the Code when it considered the question of the validity of the two charge transactions in the case, nor did it discuss them. Therefore, any opinion expressed by *Feyen* on the validity of a charge must necessarily be *obiter*.

Relying upon the decision of the Court of Appeal in the present case, an attempt was made to re-open the decision in *Feyen (supra)*. That attempt was repelled. In *Co-operative Central Bank Ltd (In receivership) v. Feyen Development Sdn Bhd.* [1997] 3 CLJ 365 *("Feyen No. 2")* this court speaking through Edgar Joseph Jr. FCJ, said (at p. 375):

> With respect, anyone reading the judgment of the Court of Appeal in *Harta Empat* should not be blamed if he is left with the distinct impression that it was an indirect attempt at resurrecting the decision in *Che Wan Development Sdn Bhd v. Co-operative Central Bank Bhd* [1992] 2 MLJ 365 – a decision which had been expressly overruled in *Feyen*. For the avoidance of doubt, we have to point out that *Che Wan*, which had been interred by *Feyen*, remains interred – in other words, remains overruled.

> For the various reasons stated, having carefully studied the judgment of the Court of Appeal in *Harta Empat,* we are not persuaded to depart from anything we had said in *Feyen* and so, even assuming for one moment that we have the power to rectify, there is nothing for us to rectify. In short, whilst we are not at liberty to overrule *Harta Empat* since it is the subject of a pending application for leave to appeal to the Federal Court, we are at liberty to say – and we do say – that in our view, the decision in *Harta Empat,* cannot stand with our decision in *Feyen.*

In an earlier passage in the same judgment, this court made clear the need to observe with rigour the doctrine of *stare decisis.* It is a passage (at p. 835) which merits reproduction:

> In *Harta Empat,* the Court of Appeal in effect held that *Feyen* was not binding on it because it had overlooked certain provisions of the Code, to wit, ss. 241(3) and 301(c). It was on the basis of this that the Court of Appeal relegated *Feyen* to mere *obiter dicta.* It is elementary that where, for example, a statute or a rule having statutory effect which would have affected the decision was not brought to the attention of the earlier court, the decision will have been given *per incuriam* (see the third exception, per Lord Green MR in *Young v. Bristol Aeroplane Co Ltd* [1944] 1 KB 718). On the other hand, *obiter dictum* is a mere chance remark by the court and is used in contradistinction to *ratio decidendi* – the rule of law for which a case is authority. Clearly, the Court of Appeal meant to say that our decision in *Feyen* was given *per incuriam.*
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> The question therefore arises: is it open to an intermediate court of appeal, such as the Court of Appeal in this country, to disregard a judgment of a final court of appeal such as the Federal Court on the ground that it was given *per incuriam*?
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> Our task in answering this question has been made considerably easier by the assistance derived from the remarks of Lord Hailsham in *Cassell & Co Ltd v. Broome & Anor* [1972] AC 1027, which indicated the reaction of the House of Lords to the Court of Appeal's refusal to follow a previous decision of the House on the ground that it had been given *per incuriam.*
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> Touching on the repercussions of the Court of Appeal advising judges of first instance to ignore decisions of the House of Lords, Lord Hailsham said this (at p. 1054B-D):
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> > I am driven to the conclusion that when the Court of Appeal described the decision in *Rookes v. Barnard* as decided '*per incuriam*' or 'unworkable', they really only meant that they did not agree with it. But, in my view, even if this were not so, it is not open to the Court of Appeal to give gratuitous advice to judges of first instance to ignore decisions of the House of Lords in this way and, if it were open to the Court of Appeal to do so, it would be highly undesirable. The course taken would have put judges of first instance in an embarrassing position, as driving them to take sides in an unedifying dispute between the Court of Appeal or three members of it (for there is no guarantee that other Lord Justices would have followed them and no particular

> reason why they should) and the House of Lords. But, much worse than this, litigants would not have known where they stood. None could have reached finality short of the House of Lords and in the meantime, the task of their professional advisers of advising them either as to their rights, or as to the probable cost of obtaining or defending them, would have been, quite literally, impossible. Whatever the merits, chaos would have reigned until the dispute was settled, and, in legal matters, some degree of certainty is at least as valuable a part of justice as perfection.

And in a famous passage (at p. 1054D-E), Lord Hailsham concluded this part of the case by saying:

> The fact is, and I hope that it will never be necessary to say so again, that in the hierarchical system of courts which exists in this country, it is necessary for each lower tier, including the Court of Appeal, to accept loyally the decisions of the higher tiers. Where decisions manifestly conflict, the decision in *Young v. Bristol Aeroplane Co Ltd* [1944] 1 KB 718 offers guidance to each tier in matters affecting its own decisions. It does not entitle it to question considered decisions in the upper tiers with the same freedom.

In our view, every word of what Lord Hailsham said regarding the status of judgments and relevance of precedent in the House of Lords, the circumstances, the duty of the Court of Appeal to accept loyally the decisions of the House of Lords and the chaotic consequences which would follow should the Court of Appeal fail in this duty apply with full force, *mutatis mutandis*, to this country and we adopt what his Lordship said. Clearly, the Court of Appeal in *Harta Empat* flew in the face of the principles enunciated by Lord Hailsham and we can only express the hope that it will not be necessary for the Federal Court hereafter to have to remind the Court of Appeal of those principles.

After the decision in *Feyen No. 2 (ibid)*, had been handed down, the defendant in the present instance successfully applied for and obtained leave to appeal against the decision of the Court of Appeal. Pursuant to that order this appeal was argued before us.

In the instant appeal a further attempt has been made by the plaintiff to resurrect the decision in *Che Wan Development (supra)* and to reverse *Feyen No. 1*. In my judgment, this attempt must fail for two reasons.

First, I do not think, as a matter of policy, it open to us to reverse a decision of another division of this court given so recently. Great care must be taken especially in a case as the present which concerns the interpretation of a statutory provision. It should not be done save in the most exceptional of cases. Otherwise it would lead to uncertainty. Men of business must be in a position to organise their affairs in such a fashion that they keep well within the framework of the law. And members of the legal profession must be able to advise their clients with some degree of certainty as to what the law is upon a particular subject matter. Certainty in the law is therefore one of the pillars upon which our justice system rests.

But I am not to be taken as saying that we should never depart from an earlier decision of this court. Departure may be warranted in a case where it appears patently clear that the earlier decision was given in defiance of an express statutory provision that was overlooked by this court. Equally where a serious error is embodied in a decision of this court that has distorted the law, in which case the sooner it is corrected the better. See, *R v. Shivpuri* [1986] 2 All ER 334. I hasten to add that that is not the position here.

I would add that, in my judgment, the reason of policy for us not to depart from *Feyen No. 1* is further strengthened by the very recent decision of this court in *Lori (M) Bhd. (Interim Receiver) v. Arab-Malaysian Finance Bhd.* [1999] 2 CLJ 997. It was there held, effectively overruling *Chung Khiaw Bank Ltd v. Hotel Rasa Sayang Sdn Bhd* [1990] 1 CLJ 675, that s. 67(6) of the Act, which is in *pari materia* with s. 133(5), has the effect of saving any security given in breach of s. 67(1). Since two similarly worded provisions in the Act have been given the same construction, any departure from *Feyen No. 1* in the present case would, I am certain, throw doubt upon the correctness of the decision in *Lori (M) Bhd. (Interim Receiver) v. Arab-Malaysian Finance Bhd. (ibid)*. Hence, much confusion and uncertainty will follow if we do anything to disturb the *status quo.*

Second, and more importantly, having read the judgment of this court in *Feyen No. 1 (supra)*, I find myself in entire agreement with the reasoning there contained. It would be surplusage to regurgitate what was there said in support of the conclusion that s. 133 does not invalidate a security given in contravention of that provision. For the purpose of the present appeal it is sufficient to reproduce the following passage in the judgment of Edgar Joseph Jr. FCJ, in *Feyen No. 1* (at p. 314) which reflects my own views upon the point in issue:

> In our view, to admit the defence of illegality to a commercial transaction of the present sort, would defeat a purposive interpretation of sub-ss. (1) and (5) of s. 133 of the Act which is designed for the protection of the company, its shareholders and creditors from unlawful dissipation of its resources.
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> We would go further and say that to admit the defence of illegality to defeat the chargee society's application to enforce the charges by way of an order for sale, would, in the words of Mason J (as he then was) in *Yango Pastoral* (at p. 428), provide 'a windfall gain' to the chargor company and others in a similar position. In consequence, such a result would impose substantial hardship upon the chargee society for, in the words of Gibbs CJ in *Yango Pastoral* (at p. 415, para 1):
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> > … if a body corporate were unable to recover money that it has lent, it would be disabled from performing its own obligations, including those owed to its depositors. In those circumstances 'the avoidance of the contract would cause grave inconvenience and injury to innocent

members of the public without furthering the object of the statute' (*Archbolds (Freightage) Ltd v. S Spanglett Ltd* [1961] 1 QB at p. 390; *Dalgety and New Zealand Loan Ltd v. VC Imeson Pty Ltd* [1963] 63 SR (NSW) 998 at p. 1004).

This court will not be astute to lend its aid to enable the chargor company to take advantage of its own default or wrong by relying on its own breach to avoid the charge transactions and thereby escape its obligations thereunder, unless this is what the clear language of the statute is thought to require. (See for example, *Kasumu v. Baba-Egbe* [1956] 3 All ER 266 at pp. 271I-272A; [1956] 3 WLR 575 at pp. 583-584.)

But, to apply s. 133 to the present charge transactions so as to produce a result which would exempt the chargor company from the obligations incurred by it thereunder would be tantamount to applying it to commercial transactions which were free from the taint of corporate abuse which the section was designed to counter. However, we repeat, this is not a court of morals but a court of law and, if the counsel for the chargor company is correct in his contentions, he is entitled to succeed.

Fortunately, in our view, sub-s. (5) of s. 133 enables us to hold that a breach of sub-s. (1) of s. 133 does not have the result contended for by counsel for the chargor company, for the reasons hereinbefore mentioned. The case of *Co-operative Central Bank Bhd v. Syarikat Bukit Tinggi & Ors* [1991] 1 CLJ 590 was, therefore, rightly decided by Mohamed Dzaiddin J (now a Federal Court judge) in favour of the chargee, on the ground of the effect of sub-s. (5) of the Act. It follows, therefore, that the case of *Che Wan* was wrongly decided.

To summarise, our conclusion is that accepting that the charge transactions did breach s. 133(1) of the Act, no civil consequences flowed therefrom, that is to say, no voidness or unenforceability attached to the loan or the charge transactions, regard being had to the context and purpose of s. 133(1), and especially the principle underlying s. 133(5), as explained above, which regrettably the learned judge failed to take into account or to give proper weight to, with the result that his judgment cannot stand.

For the reasons stated in this judgment, I would allow this appeal and set aside the orders of the Court of Appeal. The orders made by the High Court on the respondent's summons are restored. The respondent must pay the costs of this appeal and those incurred in the Court of Appeal. The deposit lodged in court must be refunded to the appellant.

There is one final matter that requires mention. Zakaria Yatim FCJ, a member of the panel which heard this appeal retired as a judge of this court on 26 January 2000. However, well before his retirement, he had conveyed to the remaining members of the panel his concurrence with the conclusions and the reasons expressed in this judgment.